



Financial Instruments in Cohesion Policy 2014-2020:

The SME Initiative

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SME Initiative: Rational

- In the aftermath of the economic crisis, European banks have been forced to:
 - Deleverage their risky assets
 - Repair their balance sheets
 - Comply with tight regulatory requirements (Basel III, CRD IV),
- which results in:
 - reduction in the volume of lending
 - market fragmentation
 - impaired money transmission to real economy
- In this context, EU SMEs were particularly hit
- ECB President Draghi, May 2013: *"The key obstacle to a growth recovery seems to be the blocked credit channel to SMEs."*

SME Initiative: Objective

- **Increase the volume** of lending to SMEs in the EU;
- **Pooling resources:** European Structural Investment Funds (ESIF) + COSME and Horizon 2020; + Combine and fully utilise the **EIB and EIF** and possibly National Promotional Banks' capacities;
- **Providing Capital Relief to EU banks** to make them more robust and to incentivize them to extend additional loans to SMEs;
- **Act fast** and achieve significant impact to stimulate SME financing and economic growth:
 - Stimulate SME financing and economic growth;
 - Fight EU fragmentation.

Main features:

- **Article 39 CPR:** legal basis;
- **Voluntary** contribution (ERDF – EAFRD) from MS;
- **EU level instrument:** indirectly managed by the Commission and EIB for the implementation;
- **Ex-ante assessment** carried out by the EIB and Commission;
- Setting up a **single dedicated OP** at MS level;
- Significant participation is needed to create critical mass & Added Value: up to **7% of ERDF – EAFRD** per MS and capped to **EUR 8.5bn** from ESIF Funds;
- Maximum contributions from EU's COSME (175 mil) and Horizon 2020 (175 mil);
- Possible contributions from other Fis & national promotional banks and/ or private investors;
- **Various financial instruments** proposed using securitisation techniques.

SME initiatives comprises of three different options:

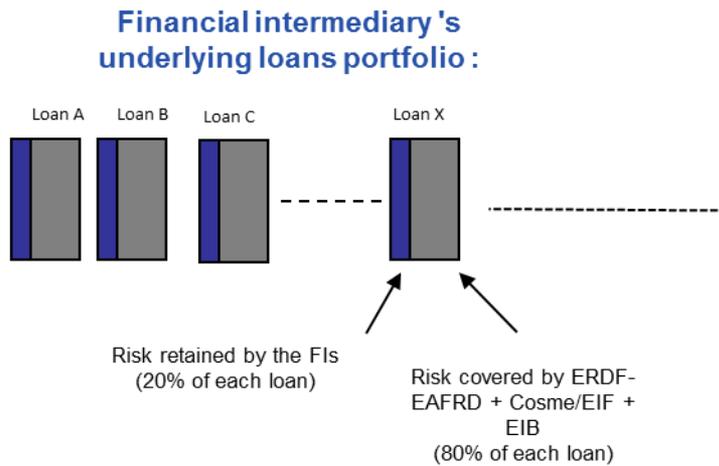
All these options are not mutually exclusive:

- **Option n°1:** Uncapped guarantee instrument;
- **Option n°2:** Joint securitisation instrument for new and existing loans;
- **Option n°3:** Joint securitisation instrument for new and existing loans and pooling the risk;

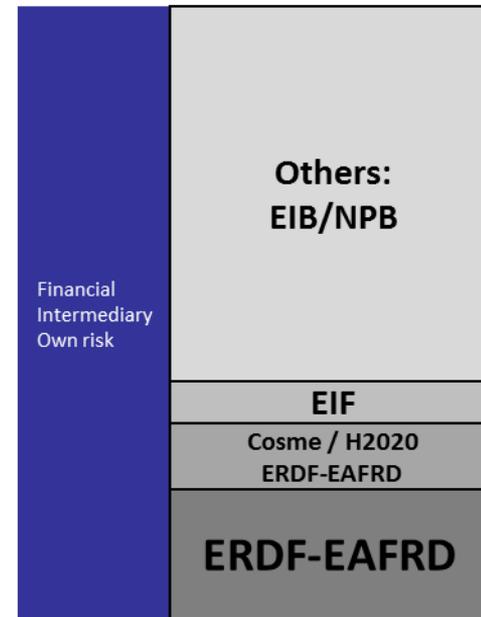
1. Uncapped Guarantee Instrument

- Combines ERDF-EAFRD, COSME, Horizon 2020 in one instrument;
- EIF, EIB and NPBs share the residual risk;
- The instrument covers 80% of the losses from the banks' portfolios;
- Alignment of interest with the bank that retains 20% risk exposure;
- Contributions from MA remain ring-fenced to support SMEs in their respective (region or) country;
- Benefit passed onto SMEs:
 - **lending to riskier SMEs (e.g. innovative SMEs, start-ups, etc.);**
 - **reduction of collateral requirements and reduced pricing.**
- Gradual capital relief to financial intermediaries to support new lending to SMEs.

Uncapped guarantee: Option 1

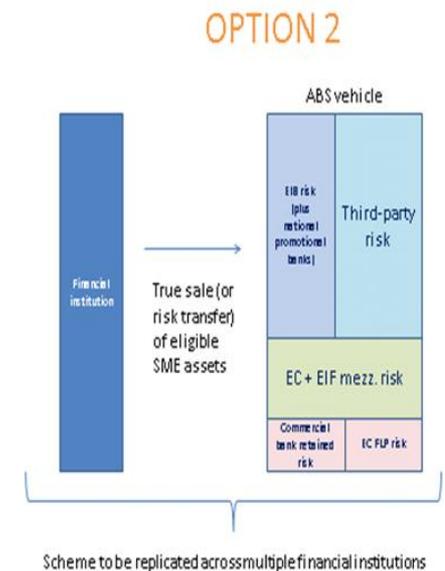


New debt finance portfolio



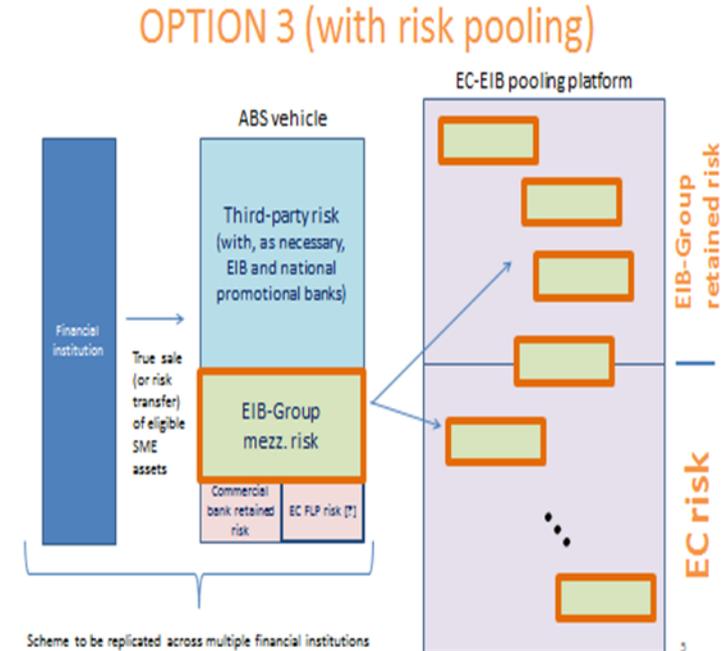
2. Joint securitisation instrument for new and existing loans

- Combining resources from ERDF-EAFRD, COSME, Horizon 2020, EIF, EIB and possibly NPBs in one instrument;
- Two steps: a) securitisation of an existing/new portfolio and b) construction by the bank of a new portfolio;
- Increase lending to SMEs by providing capital relief and/or liquidity to on-lending banks
- ERDF-EAFRD take 50% of the riskier tranche (Junior tranche);
- Bank would retain a material interest in the transaction (adequate portion of the Junior tranche appx. 50%) to help ensuring alignment of interest and good origination standards;
- EU resources together with EIF own resources guarantee the Mezzanine tranche
- EIB and other institutional investors invest in the Senior tranche.



3. Joint securitisation instrument for new and existing loans with risk pooling

- Similar to option2 but it includes the concept of pooling ESIF resources and risks;
- Pooling is limited to the mezzanine tranche insofar as FLP is covered by each originator and by each MS contribution (ERDF-EAFRD);
- High number of countries and contribution are preconditions for option n°3 (ensure appropriate diversification + involvement of private investors).



Main result of the ex-ante assessment:

- **At the EU28 level**, the ex-ante assessment by using a conservative approach estimates that
 - up to 4.1% of all SMEs were unsuccessful in obtaining loan finance even though "financially viable",
 - i.e. approximately up to 860,000 SMEs,
- The EU-wide **loan financing gap** for the non-financial sector in the period 2009-2012 is quantified at up to EUR 112 billion,
- The future evolution of the SME gap financing in the EU28MS will likely improve, **however that reduction will be far from sufficient to fill the loan financing gap.**

Country fiche for Spain:

MACROECONOMIC INDICATORS

GDP GROWTH RATE (2013):	-1.3%	LOANS-TO-DEPOSIT RATIO (2012):	92.4%
OUTPUT GAP (2013):	-5.2%	NON-PERFORMING LOANS RATIO (2012):	7.1%
UNEMPLOYMENT RATE (2013):	26.6%	BANK CAPITAL ADEQUACY RATIO (2012):	11.4%
GOVERNMENT NET LENDING / BORROWING (2013) AS % OF GDP:	-6.8%	RETURN ON BANK EQUITY (2012):	-2.9%
GROSS GOVERNMENT DEBT (2013):	94.8%	CENTRAL BANK LIQUIDITY AS % OF LIABILITIES (2012):	12.0%
CORPORATIONS NET LENDING/BORROWING (2013) AS % OF GDP:	6.4%	BANKS' EXPOSURE TO VULNERABLE COUNTRIES (2012):	6.2%
SOVEREIGN INTEREST RATES SPREAD VERSUS BUND (2012):	4.4%	FOREIGN OWNERSHIP OF THE BANKING SYSTEM (2009):	10.2%

FINANCIAL INDICATORS FOR SMES

SHARE OF SMES OVER TOTAL ENTERPRISES (2013):	99.9%	SMAF DEBT SUB-INDEX (2011):	103.0
SHARE OF SME EMPLOYMENT (2013):	75.4%	NUMBER OF INITIATIVES SUPPORTING LOANS UNDER STRUCTURAL FUNDS (2007 - 2013):	5
SHARE OF BANK LOANS TO SMES OVER TOTAL (2007-2011):	34.6% [§]	GROWTH IN SME LOANS (2007 - 2011):	-55.8% [§]
SHARE OF SME LOANS IN TOTAL SME DEBT (2012):	73.5%	INTEREST RATE SPREAD FOR SME LOANS (2012-12):	1.06%
SHARE OF DISCOURAGED SMES (2012H2):	10.0%	AVERAGE LOAN SIZE PER SME (2009 - 2012):	EUR 223,000

SHARE OF FINANCIALLY VIABLE SMES UNSUCCESSFUL IN OBTAINING LOAN FINANCING (2011H2-2012H2):	21.8%	ESTIMATED INTERVAL FOR SME LOAN FINANCING GAP (2011 - 2012):	6,003 - 26,397 € Mln
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- Difficult macroeconomic situation (GDP & unemployment rate)
- SMEs make up **99.9%** of enterprises
- SMEs account for **75.4%** of employment workers
- SMEs loan have shrunk by **11.2%** (2007-2011)
- The trend of SMEs unsuccessful in obtaining loan is increasing **+21.8%**
- Debt financing gap ranging between **EUR 6,003m - EUR 26,397m**

SME Initiative : Next steps

- Each participating Member shall provide the COM with a **single dedicated national programme** per financial contribution by ERDF and EAFRD supporting the thematic objective set out in Article 9 (3) i.e. supporting the capacity of SMEs to grow in regional, national and international markets, and in innovation processes;
 - **The resources for implementing the SME Initiative at regional level should be provided under the single dedicated national programme (e.g. critical mass required).**
 - **If contributions at regional level (covering several regions), then the Single dedicated national Programme shall highlight the appropriate amounts by regions. Contributing regions shall agree to designate a "single authorities" as: managing authority, certifying authority (where applicable), audit authority.**
- Approval of the Single dedicated national programme by the COM.
- Commission shall adopt by means of an implementing act a model of the funding agreement

- Negotiation of the funding agreement between the participating MS and the EIB.
 - **Positive: Signature of the Funding Agreement (the signature shall occur within 6 months following the approval of the single dedicated national programme by the COM). If SME Initiative set up at regional level, this should be clearly specified in the dedicated programme and in the FA;**
 - **Negative: Member State shall submit a request for amendment of the single dedicated national programme and reallocate the contribution to other programmes and priorities in accordance with requirements for thematic concentration.**

- Request for payment from the EIB to the participating MS.

- Transaction approved with the selected financial intermediary (this approval should occur within 3 months following the request for payment from the EIB to the participating MS).

Q&A session

- *Added value*
- *Regional implementation*
- *Top-up*
- *Single dedicated national programme*
- *Request for payment & Timing*
- *Leverage*
- *Way out if it does not work*
- *Governance*

Added value

*At the level of participating **Member States***

- no national co-financing required for the contributions from ESIF
- Leverage effect on the ESIF contribution by a combination of resources
- fast deployment of the Initiative
- higher number of SMEs supported and more beneficial terms for SMEs thanks to risk-sharing with the EU and EIB Group
- Complement the existing financial instruments to address market failure

*At the level of **financial intermediaries***

- capital relief enabling new debt finance to SMEs
- additional funding in case of true securitization
- Extend volume of loans without impacting on risk exposure

*At the level of **SMEs***

- more liquidity for investments,
- improved financing conditions and
- better terms of loan contracts with financial intermediaries
- Availability of financing for projects that would otherwise be turned down by banks

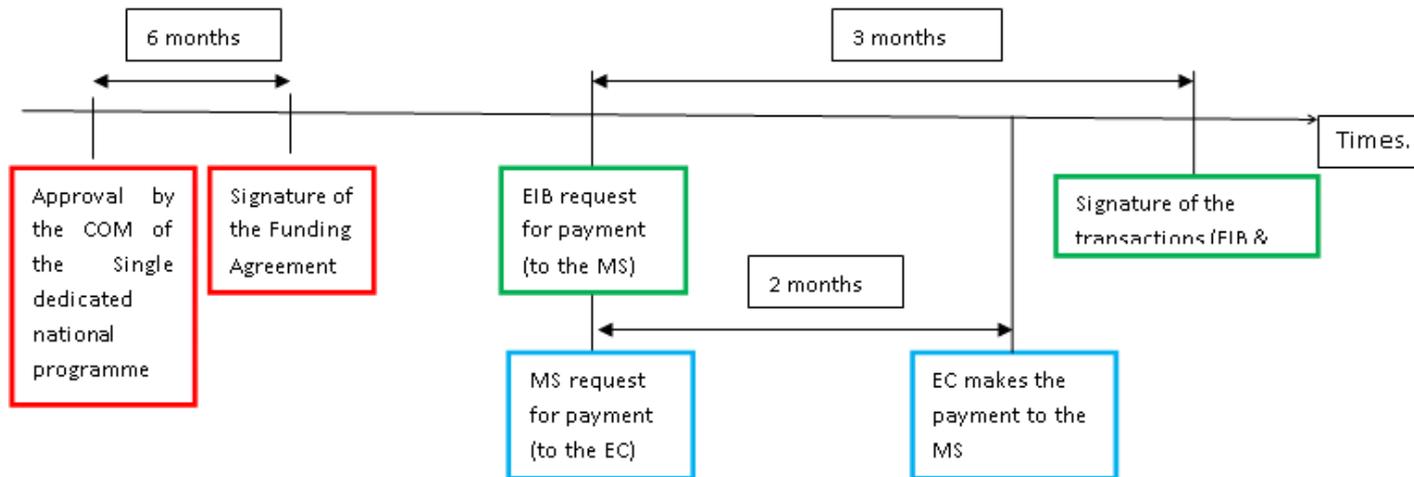
Regional implementation & Top up

- Main objective is to be efficient then "**critical mass**" is a prerogative (*All options have to rely on a sufficient commitment to roll out the instrument*);
- Keeping in mind this first point: it should also be possible to allow for a pro-rata return to a region or group of regions within the same Member State (Article 39 paragraph 11 CPR);
- Regional implementation should be clearly mentioned in the single dedicated national programme & Funding Agreement per financial contribution by the ERDF and EAFRD;
- Part of the negotiation of the Funding Agreement with the EIB-Participating Regions (critical mass required);
- Provided that the condition of "critical mass" is met, it is not excluded that the Region(s) would be able, under certain conditions, to top up their initial contribution at a later stage.

Single dedicated national programme

- CPR (Article 97) foresees a **specific provisions** regarding the programming of support;
- The Single dedicated national programme **shall include** only:
 - points (i), (ii) and (iv) of Article 96 (2)(b),
 - point (d) of Article 96(2),
 - paragraph (5) of Article 96 and
 - point (b) of Article 96(6).
- **Model** for the operational programme will be adopted by an implementing act.

Request for payment & timing



- MS request for payment to the EC shall be made on the basis of 100% of the amounts to be paid by the MS to the EIB.
- In the FA the MS will defined with EIB a schedule regarding the timing when money to be paid by the MS to the EIB.
- Regarding the timing needed to transfer the money from EC to MS, according to CPR the Commission shall make the interim payment no later than 60 days after the date on which a payment application is registered with the Commission.

Leverage:

Def. in CPR: Ratio between the new debt finance to eligible SMEs to be originated by the financial intermediaries and the corresponding contribution of the ERDF and EAFRD from the relevant Member State to the financial instruments.

OPTION 1	%	EUR
Class B + Senior	57%	285.00
EIF	2.0%	10.00
ERDF/Cosme/H2020	8.0%	40.00
ERDF	13.0%	65.00
Total covered	80%	400.00
Total bank own risk	20%	100.00
Total amount of the portfolio	100.0%	500.00
Total ERDF/Cosme/H2020		105.00
ERDF	98%	102.90
Cosme/H2020	2%	2.10
Leverage		4.86
Total amount of the portfolio		500.00
out of which SMEs in line with COSME/H2020	20	42.00

Expected leverage on average for Option n°1: **5x**

OPTION 2	%	EUR
Step n°1: Securitised portfolio breakdown by investors		
Class B + Senior	70%	350.00
EIF	2%	10.00
ERDF/Cosme/H2020	8%	40.00
Originator	10.00%	50.00
ERDF	10.00%	50.00
Total	100%	500.00
Total ERDF/Cosme/H2020		90.00
ERDF	98%	88.20
Cosme/H2020	2%	1.8
Leverage		7.0
Step n°2: Additional portfolio		617.40
out of which SMEs in line with COSME/H2020	15	27.00

Expected leverage on average for Option n°1: **7x**

Way out if it does not work:

- Implementation of the financial instrument shall be **discontinued** and the contributions returned to the Regions when the sum of the contributions of all participating MS is insufficient (not min critical mass);
- **Reallocation** of the contribution to other programmes in accordance with the TO when the parties are not able to agree on the conditions on the MFA;
- Amendment of the programme & reallocation of the remaining contribution **if the conditions for the termination have been satisfied**; depending on the negotiation but:
 - the "non-achievement of the milestone" is not a termination event therefore, MS cannot terminate the FA and reallocate the funding elsewhere in its programming. In any case if the portfolio is not built up to the level required in the FA, the Participating MS will be entitled to receive a resources paid by the selected FI (penalty).

Governance

- SME Initiative implementation supervised by a Steering Committee;

- Steering Committee composed of:
 - Commission/EIF
 - Member States

- The EIF will act as the Secretariat of the SC;

- Role of the Steering Committee defined in the FA, e.g.:
 - Review the Call for Expression of Interest;
 - Review progress of the implementation;
 - Issue opinion and provide with some guidance;
 - Review amendments to the FA; etc.

- Regular meeting (e.g.: twice a year)

Thank you for your attention!

DG Regional and Urban Policy – Directorate B, Policy
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